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IN THE

Supreme Court of the United States

OCTOBER TERM, 1986

FEDERAL INSURANCE COMPANY & COMETALS, INC.,
Petitioners,

v.

UNITED STATES,
Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FEDERAL CIRCUIT

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QUESTIONS PRESENTED FOR REVIEW

I. THE CORRECTNESS OF THE CATEGORICAL HOLDING THAT EQUITABLE ESTOPPEL IS NEVER AVAILABLE AGAINST THE GOVERNMENT IN AN IMPORT DUTY CASE.

Given that this Court has declined to articulate a flat rule that estoppel may not in any circumstances arise against the government, can an appeals court create such a blanket rule by holding that equitable estoppel is never available in cases involving the collection of import duties?

II. THE CORRECTNESS OF THE HOLDING DENYING EQUITABLE ESTOPPEL IN THE FACE OF AN ACT OF CONGRESS FOUND BY THE TRIAL COURT TO REQUIRE GRANTING OF EQUITABLE ESTOPPEL.

Should a public policy expressed in an act of Congress and directed to protect the individual members of a class dictate that the remedy of equitable estoppel granted by the trial court to a member of that class remain undisturbed, when there is a finding of governmental affirmative misconduct and a finding of the presence of the traditional elements of estoppel?

III. THE CORRECTNESS OF THE HOLDING THAT THE COUNTERCLAIM OF RECOUPMENT FAILS FOR THE SAME REASON AS EQUITABLE ESTOPPEL IN LIGHT OF THE RECENTLY ESTABLISHED STATUTORY SCHEME PERMITTING COUNTERCLAIMS IN THE COURT OF INTERNATIONAL TRADE.

Is the counterclaim of recoupment against the government permitted by the Customs Courts Act of 1980, a separate and distinct defense from equitable estoppel?

LIST OF PARTIES

The parties to the proceedings in the United States Court of Appeals for the Federal Circuit were Federal Insurance Company;[1] Cometals, Inc. and the United States.

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[1] Federal Insurance Company was the surety for Cometals, Inc. in the import transaction herein.

TABLE OF CONTENTS

	Page
QUESTIONS PRESENTED	i
LIST OF PARTIES	ii
TABLE OF AUTHORITIES	v
OPINIONS BELOW	1
JURISDICTION	2
STATEMENT OF THE CASE	2
Proceedings in the Court of International Trade	6
Proceedings in the Court of Appeals for the Federal Circuit	9
REASONS FOR GRANTING THE WRIT	11
I. The Holding Of The CAFC In Prohibiting Equitable Estoppel Against The Government In Import Duty Cases Conflicts With The Expressions Of This Court And Other Circuit Courts Of Appeals.	11
II. The Holding Of The CAFC Prohibiting Equitable Estoppel Against The Government Involves An Important Question Of Law Which Has Not Been Settled By This Court.	13
III. The Petition Should Be Granted To Carry Out Congress' Intent to Permit Counterclaims Against the Government in Import Transactions.	17
CONCLUSION	19
APPENDICES	1a
Appendix A. Opinion of the Court of Appeals for the Federal Circuit	1a
Appendix B. Order of the Court of Appeals for the Federal Circuit denying rehearing in banc	28a

Appendix C. Opinion of the Court of International Trade (March 14, 1985) 29a

Appendix D. Opinion of the Court of International Trade (November 15, 1983) 45a

Appendix E. 19 U.S.C. §1641 ..... 48a

Appendix F. 19 U.S.C. §1648 ..... 52a

Appendix G. 28 U.S.C. §1583 ..... 53a

Appendix H. 19 C.F.R. §24.1(3) (1980) 54a

Appendix I. 19 C.F.R. §111.27 (1980) 55a

Appendix J. 19 C.F.R. §111.29 (1980) 56a

TABLE OF AUTHORITIES

CASES: Page

Brandt v. Hickel, 427 F.2d 53 (9th Cir. 1970) ... 13

Corneil-Rodriguez v. Immigration and Naturalization Service, 532 F.2d 301 (2d. Cir. 1976) 13,16

Emeco Industries, Inc. v. United States, 485 F.2d 652 (Ct. Cl. 1973) 13

Frederick v. United States, 386 F.2d 481 (5th Cir. 1967) 17,19

Heckler v. Community Health Services of Crawford County Inc., 467 U.S. 51 (1984) 11,12,13

Meister Brothers, Inc. v. Macy, 674 F.2d 1174 (7th Cir. 1982) 13

United States v. Georgia-Pacific Co., 421 F.2d 92 (9th Cir. 1970) 13

United States v. Lazy FC Ranch, 481 F.2d 985 (9th Cir. 1973) 13

United States v. Locke, 471 U.S. 84 (1985) 11,12,13

United States v. Ruby Co. 588 F.2d 697 (9th Cir. 1978) 7

STATUTES:

Administrative Procedure Act, 5 U.S.C. 701 *et seq* 6

Customs Courts Act of 1980, 28 U.S.C. 1581 *et seq* i,18

Federal Tort Claims Act, 28 U.S.C. 2671 *et seq* 6

Tucker Act, 28 U.S.C. 1491 *et seq* 6

19 U.S.C. §1641 ..... *passim*

19 U.S.C. §1648 2

28 U.S.C. §1254 (1) 2

28 U.S.C. §1582 6,19

28 U.S.C. §1583 2,18,19

Table of Authorities Continued

	Page
REGULATIONS:	
19 C.F.R. §24.1(3) (1980)	2,7,9
19 C.F.R. §111.27 (1980)	2,5,8,15
19 C.F.R. §111.29 (1980)	2,15
19 C.F.R. §142.4 (1980)	6
19 C.F.R. §142.25 (1980)	5
19 C.F.R. §142.27 (1980)	5
RULES:	
Federal Rules of Civil Procedure Rule 13	17
MISCELLANEOUS:	
Customs Courts Act of 1979, S. 1654: Hearings on S.1654 Before the Subcommittee on Improvements in Judicial Machinery, 96th Cong. 1st. Sess. (1979)	18
S. Rep. No. 1170, 74th Cong., 1st. Sess. (1935)	8,14
H. Rep. No. 96-1235, 96th Cong., 2d Sess. 61 (1980)	19
67 Cong. Rec. 7497 (1910)	14
United States Customs Service, *Customs Brokers Automated Survey* (February 13, 1981)	3
United States Customs Service Headquarters Task Force on Customhouse Brokers (Interim Task Force Report (1977))	3,4

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v.

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Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FEDERAL CIRCUIT

Petitioners, Federal Insurance Company and Cometals, Inc. respectfully pray that a writ of certiorari issue to review the judgment of a divided (2-1) panel of the United States Court of Appeals for the Federal Circuit ("CAFC") entered on November 10, 1986, reversing the judgment of the Court of International Trade in petitioners' favor. A petition for rehearing in banc was denied by the CAFC on December 8, 1986.

OPINIONS BELOW

The majority and dissenting opinions and the order of the CAFC are reported at 805 F.2d 1012 (Fed.

Cir. 1986). (Appendix A, 1a-27a). The order of the CAFC entered December 8, 1986 denying rehearing in banc is not reported and was not accompanied by any opinion. (Appendix B, 28a). The opinion of the Court of International Trade, *per* Watson, *J.*, entering judgment in favor of petitioners is reported at 605 F. Supp. 298 (Ct. Int'l Trade 1985). (Appendix C, 28a-44a). In an earlier opinion, the Court of International Trade dismissed petitioners' counterclaims other than equitable counterclaims. This decision is reported at 6 CIT 243 (1983). (Appendix D, 45a-47a).

JURISDICTION

The judgment of the CAFC was entered on November 10, 1986. The motion for rehearing was denied on December 8, 1986. This petition was filed within ninety days of the latter date. This Court's jurisdiction is invoked under 28 U.S.C. §1254(1).

STATUTORY AND REGULATORY PROVISIONS INVOLVED

The statutory and regulatory provisions relevant to this case, 28 U.S.C. §1583, 19 U.S.C. §1641, 19 U.S.C. §1648, 19 C.F.R. §24.1(3) (1980), 19 C.F.R. §111.27 (1980) and 19 C.F.R. §111.29 (1980) are reprinted in Appendix E through J, respectively, (48a-56a).

STATEMENT OF THE CASE

Background

According to the latest survey prepared by the United States Customs Service, approximately 96.7% of all commercial entries are handled for importers

by customs brokers.[2] Customs brokers assist the importers in entering goods, filing necessary papers and submitting the appropriate fees on behalf of importers.

The licensing and supervision of customs brokers is in accordance with a statutory and regulatory scheme enacted in 1910. In 1935, after lengthy hearings in which testimony to the effect that certain fraudulent practices by brokers existed which threatened the revenue of the United States as well as the importer, Congress amended 19 U.S.C. §1641 to insert the following language:

> Sec. 1641(d) The Secretary of the Treasury shall prescribe such rules and regulations as he may deem necessary *to protect importers and the revenue of the United States. . . .* [Emphasis added]

In 1977, the Customs Headquarters Task Force on Customhouse Brokers in an Interim Task Force Report rejected a suggestion that customs brokers be deregulated and stated that:

> . . . licensing (and regulation) of customhouse brokers is beneficial to both the Customs Service and the importing community and . . . stronger regulation is needed.
>
> . . .
>
> *A license implies a certain standard of performance and acceptable level of integrity and accountability. The public expects the licensee*

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[2] United States Customs Service, Office of Automated System Operations, *Customs Brokers Automation Survey*, ADP-1-CM:D:B RB (February 13, 1981).

> *to be competent, honest, and endorsed by the Government.* A license issued without regulations to control the licensee would be a disservice to the importing public and to Customs.

Interim Task Force Report at 2.

The Customs Service recognized its responsibility to both license and regulate customs brokers and acknowledged that "*it would almost be misleading to the public not to regulate those licensees fully and effectively and enforce our requirements.*" *Id.* at 3. (Emphasis supplied)

Significantly, the Customs Service Task Force found in 19 U.S.C. §1641 authority to make a requirement by regulation that brokers post bonds. The suggested regulatory change was viewed as a means of guaranteeing the protection of importers and the government in situations where a broker had mishandled client funds.

Facts

This action arose out of the importation on May 7, 1980 by Cometals, Inc. ("Cometals") of titanium sponge at the port of Los Angeles, California. As a result of the entry of this merchandise, Cometals owed $230,344.12 in import duties to the government. The documents relating to the importation of the merchandise into the United States were filed by Cometals' licensed United States Customs broker, James Loudon & Co., Inc. ("Loudon").

In October 1977, the Customs Service had, without the knowledge of the petitioners, audited Loudon and found "a severe net worth deficiency." (Appendix A, at 6a). The Customs Service audit also found that

Loudon was responsible for more than $190,000.00 in overdrafts. Moreover, in 1979 and 1980, prior to the entry of the merchandise in this case, six of Loudon's uncertified checks covering import duties for previous Cometals' entries were returned to the government for insufficient funds. (Appendix A, at 6a). Petitioners were not apprised of any of these disturbing facts by the Customs Service.[3] Nor was any Customs audit conducted on Loudon between 1977 and the transaction in question despite the Customs Service's obligation to do so pursuant to 19 C.F.R. §111.27.[4]

On May 2, 1980, Cometals transmitted to Loudon the necessary funds to pay the customs duties for the import entry in question. Thereafter, on May 12, 1980 Loudon tendered an uncertified check in the amount of $230,344.12 to the United States Customs Service for payment of these duties owed by Cometals.

Loudon's first check was returned due to insufficient funds, at which time the Customs Service asked

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[3] The Customs Service could have given actual or constructive notice by issuance of a demand for liquidated damages when Customs duties were not promptly paid or by withdrawing immediate delivery privileges. *See* 19 C.F.R. §142.25 and 19 C.F.R. §142.27 (1980).

[4] Both the Court of International Trade and the CAFC are of one mind regarding the Customs Service's obligation to conduct such audits in the circumstances of this case. In fact, the *CAFC unequivocally states that: "[W]here the government is aware that a broker is in a precarious financial condition or has mishandled the affairs of importers, the government is obliged to investigate and in appropriate circumstances, to suspend or revoke the license of such broker."* [Appendix A, at 3a] Similarly, the Court of International Trade found that the failure to investigate Loudon in these circumstances was affirmative misconduct. [Appendix C, at 37a].

for and received a second check from Loudon, which was also returned for insufficient funds. After further demands by the Customs Service on Loudon proved futile, the Customs Service turned to Cometals and its surety, Federal Insurance Company, for payment.[5]

Petitioners refused to pay claiming that the affirmative misconduct of the Customs Service in not complying with its own regulations was the only reason Customs did not collect the duties.

Proceedings in the Court of International Trade

In May 1982, the Customs Service brought suit against petitioners in the United States Court of International Trade to recover the Customs duties. Jurisdiction was based on 28 U.S.C. §1582. Cometals and Federal Insurance Company claimed that the Customs Service was equitably estopped from collecting the duties in question a second time from petitioners due to its affirmative misconduct in not fulfilling its congressionally mandated obligations to supervise Loudon's financial integrity.[6]

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[5] Cometals, as a regular importer of merchandise had a term bond, issued by Federal Insurance Company, on file with the United States Customs Service to cover payment for duties, fees, liquidated damages etc. which may accrue during the importing process. *See* 19 C.F.R. §142.4 (1980).

[6] Petitioners also asserted a number of counterclaims. These claims under the Federal Tort Claims Act (28 U.S.C. §2671 *et seq.*), the Tucker Act (28 U.S.C. §1491 *et seq.*), and the Administrative Procedure Act, (5 U.S.C. §701 *et seq.*), were dismissed by the court. The counterclaim of recoupment was not dismissed by the Court of International Trade. *United States v. Federal Insurance Company and Cometals Inc.*, 6 CIT 243 (1983). [Appendix D, at 47a].

The Court of International Trade held for petitioners.

It found that "sole responsibility for not receiving the duties that are claimed to be owed by the defendants [petitioners], must be attributed to the plaintiff's [the government's] malfeasance." (Appendix C, at 30a). The court found the traditional elements of estoppel were "clearly present in the instant action."[7] (Appendix C, at 38a).

Furthermore, the Court of International Trade found the presence of the additional element of affirmative government misconduct in this case in that the government "failed to comply with the law and ignored the public interest by not protecting *both* importers *and* the revenue of the United States." (Appendix C, at 40a) (Emphasis in original)

The Court of International Trade held that this affirmative misconduct consisted of two independent elements. First, the Customs Service improperly relied upon petitioners' bond to guarantee the payment of the uncertified check of the customs broker in violation of 19 C.F.R. §24.1(3). (Appendix H, at 54a). Second, the Court of International Trade held that in failing to conduct audits of the broker for three years, as it was required to do by law, the Customs Service

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[7] The Court of International Trade found that a) the Customs Service was the only party to know all the facts; b) the Customs Service intended or knew that petitioners would rely on the government's compliance with the law; c) petitioners were unaware of these facts and; d) petitioners, in transmitting funds to Loudon to pay duties, relied upon the Customs Service's violation of law to their detriment. *See United States v. Ruby Co.*, 588 F.2d 697, 703 (9th Cir. 1978).

was placing its interests and the interests of importers at increasing risk, precisely those risks Congress intended to avoid when enacting 19 U.S.C. §1641 *et seq.*[8] *See also* 19 C.F.R. §111.27. (Appendix I, at 55a).

The Court of International Trade found that both these provisions were mandated by Congress under 19 U.S.C. §1641 to protect both the revenue of the United States and importers against fraudulent financial practices by licensed customs brokers. *See* S. Rep. No. 1170, 74th Cong., 1*st* Sess., 3 (1935). (Appendix C, at 34a).

Accordingly, the court held that by not auditing Loudon and by continuing to accept Loudon's uncertified checks while knowing that Loudon was insolvent and that Loudon's checks had a history of being returned for insufficient funds, the Customs Service was solely responsible for the failure to collect the duties which Cometals paid. The Court of International Trade stated:

> *The Regional Director must conduct audits in a manner designed to protect both importers and the revenue of the United States. This Court cannot permit the plaintiff to ben-*

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[8] 19 U.S.C. §1641(d) states in pertinent part:

> The Secretary of the Treasury shall prescribe such rules and regulations as he may deem necessary to *protect importers and the revenue of the United States . . . including rules and regulations requiring the keeping of books, accounts, and records by customhouse brokers, and the inspection thereof,* and of their papers, documents, and correspondence by, and the furnishing by them of information relating to their business to any duly accredited agent of the United States. [Appendix E, at 51a]. [Emphasis supplied].

> *efit from its own violation of the law nor can it condone the Customs Service's failure to conform to its own regulations.* By continuing to redeposit Loudon's "bouncing checks" in early 1980, the government was directly responsible for endangering the payment of duties by Cometals. At the same time, the government was not enforcing a law intended to protect *both* importers and the revenue of the United States. [Appendix C, at 37a]. [Emphasis partially supplied]

Proceedings in the CAFC

The government appealed the Court of International Trade's decision to the CAFC. A divided three judge panel of the CAFC reversed, with Judge Newman filing a dissent. The CAFC held that equitable estoppel is *never* available against the government in a case involving the collection of import duties. (Appendix A, at 3a).

Furthermore, the CAFC rejected, as a matter of law, the holding that the Customs Service committed affirmative misconduct as to the first element of such misconduct found by the Court of International Trade, i.e. the Customs Service's acceptance of the broker's uncertified check secured by the importer's bond. The CAFC held that the government's interpretation of the regulation 19 C.F.R. §24.1(3), was both longstanding and reasonable.

However, as to the second element of affirmative misconduct found by the Court of International Trade, i.e. failure to conduct an audit of the broker for three years after being alerted to repeated misconduct, overdrafts and other abuses, the CAFC had only this to say:

> Where the *government is aware that a broker is in a precarious financial condition or has mishandled the affairs of importers, the government is obliged to investigate* and, in appropriate circumstances, to suspend or revoke the license of such broker. [Appendix A, at 3a]. [Emphasis supplied]

Having found that the Customs Service was obligated to investigate and take remedial action in this case, the CAFC did not disturb the Court of International Trade's finding that the government committed affirmative misconduct by not conducting such an audit. Thus, the Court of International Trade's finding and holding that the government committed affirmative misconduct in this case[9] has never been disturbed on appeal.

Circuit Judge Newman filed a strong dissent stating that since the facts were not in dispute there was nothing warranting the disturbance of the Court of International Trade's discretion in granting the equitable relief. Moreover, Judge Newman stated:

> I do not see how the presence of Cometals' bond is a sufficient excuse for the government's laxness, if not acquiescence, in Loudon's financial footwork when the Treasury regulations require the government to license only financially sound customs brokers . . .
>
> . . . The Court of International Trade held that the Customs Service was chargeable

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[9] The CAFC, in its opinion explicitly acknowledges that this was the basis for the Court of International Trade's holding in this case [Appendix A, at 6a (numbered paragraph (3))].

> with "affirmative misconduct" in not requiring a bond of Loudon and in failing to audit and determine his [its] financial responsibility, as the law and Treasury regulations require. On this record, the imposition of equitable estoppel is supported by precedent. [Appendix A, at 22a].

REASONS FOR GRANTING THE WRIT

I. The Holding Of The CAFC In Prohibiting Equitable Estoppel Against The Government In Import Duty Cases Conflicts With The Expressions Of This Court And Other Circuit Courts Of Appeals.

In this case the Court of International Trade found that the *sole* reason that the Customs Service did not collect the duties paid by Cometals was the Customs Service's affirmative misconduct. That misconduct consisted of the Customs Service's failure to supervise and control the actions of a customs broker, the government knew to be insolvent, and in accepting that broker's uncertified check in payment of duties. Because the CAFC left the Court of International Trade's finding of affirmative misconduct in relation to the failure of the government to audit and supervise the broker undisturbed, its conclusion that the government cannot be estopped in this case is contrary to law, and is in conflict with decisions of this Court and the circuit courts of appeals.

The petition should be granted to resolve this intolerable conflict between the CAFC's *per se* rule prohibiting the defense of equitable estoppel against the government in an import duty case and this Court's recent decisions in *United States v. Locke*, 471 U.S. 84 (1985) and *Heckler v. Community Health Services*

of Crawford County, Inc., 467 U.S. 51 (1984), which make it clear that under certain stringent and unique circumstances, equitable estoppel may be available as a defense against the government.[10] Explicitly underlying these holdings is the expectation of regularity and honesty that citizens have a right to expect from their government. By contrast, in this case the CAFC held that the Customs Service may never be equitably estopped when it is engaged in the collection of import duties despite its knowing violation of law.

This *per se* rule is also in direct conflict with the decisions of the circuit courts of appeals, which have held that in certain prescribed circumstances where the government has acted improperly the policy restricting the application of the doctrine of equitable estoppel must give way to the interest of the public "in seeing its government deal carefully, honestly and

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[10] In *Community Health Services*, this Court explicitly declined to say:

> . . .that there are *no cases* in which the public interest in ensuring that the Government can enforce the law free from estoppel might be outweighed by the countervailing interest of citizens in some minimum standard of decency, honor and reliability in their dealings with their Government. 467 U.S. at 60. [Emphasis in original]

In *Locke* this court remanded with specific instruction that the defense of equitable estoppel may be considered on the remand. 471 U.S. at 90 n. 7. Justice O'Connor's concurring opinion in *Locke* cited with approval the conclusion by this Court in *Community Health Services* that certain circumstances may arise which warrant the application of estoppel against the government. 471 U.S. at 111.

fairly with its citizens." *Meister Brothers, Inc. v. Macy*, 674 F.2d 1174, 1177 (7th Cir. 1982).[11]

The holding of the CAFC that estoppel is never permitted against the government in connection with import duties, even where affirmative misconduct has been found, is not supported by the decisions of this Court in *Community Health Services* and *Locke* or other circuit courts of appeals. This Court should grant this petition in order to resolve the conflict created by the CAFC.

II. The Holding Of The CAFC Prohibiting Equitable Estoppel Against The Government Involves An Important Question Of Law Which Has Not Been Settled By This Court.

This petition should be granted in order to resolve an important question of law regarding the availability of a remedy to an injured party (e.g. Cometals)

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[11] *See also Corneil-Rodriguez v. Immigration and Naturalization Service*, 532 F.2d 301 (2d Cir. 1976) (refusing "to sanction a manifest injustice occasioned by the Government's own failures"); *United States v. Lazy FC Ranch*, 481 F. 2d 985 (9th Cir. 1973) ("estoppel is available as a defense against the government if the government's wrongful conduct threatens to work a serious injustice and if the public's interest would not be unduly damaged by the imposition of estoppel"); *Brandt v. Hickel*, 427 F.2d 53 (9th Cir. 1970) ("some forms of erroneous advice are so closely connected to the basic fairness of the administrative decision making process that the government may be estopped"); *United States v. Georgia-Pacific Co.*, 421 F.2d 92 (9th Cir. 1970) ("the dictates of both morals and justice indicate that the Government is not entitled to immunity from equitable estoppel in this case"); *Emeco Industries, Inc. v. United States*, 485 F.2d. 652 (Ct. Cl. 1973) (government not immune from estoppel where its denial would be "'contrary to equity and good conscience'"). As cited by Judge Newman, dissenting. [Appendix A, at 24a].

when the government fails in its statutorily mandated responsibility to protect that specific party from acknowledged and recognizable evils (e.g. broker fraud).

Congress' intent to protect importers against the unscrupulous practices of customs brokers has been repeatedly expressed. Over 75 years ago, the first bill requiring the licensing and regulation of customs brokers was enacted for the express purpose of "driving out of business the dishonest and unscrupulous broker." 67 Cong. Rec. 7497 (1910). In the 1935 amendments to 19 U.S.C. §1641, Congress continued its efforts to protect importers and to combat broker fraud. Congress concluded that:

> *In view of the fact that these customhouse brokers are quasi officers of the Treasury and that by licensing them the Treasury holds out to importers that it has investigated their character and represents to such importers that they are capable and honest in their conduct* and in view of the large opportunities for profitable fraud open to dishonest persons . . . it is essential that the Department have wide discretion in dealing with these brokers and that the Secretary of the Treasury, therefore, be given broad powers to supervise and regulate their activities.
>
> . . .
>
> The present amendments . . . will give to the Secretary of Treasury the power to regulate the conduct of the business of customhouse brokers in such a manner that the opportunity for fraudulent practices will be reduced to an absolute minimum.

S. Rep. No. 1170, 74th Cong., 1st Sess. at 3 (1935). [Emphasis supplied]

As the Court of International Trade held, the strong public policies underlying this statutory scheme demand Customs Service enforcement of those regulations promulgated under 19 U.S.C. §1641. The government's failure to enforce those regulations and particularly to abide by the congressional mandate contained in the statute, in its dealings with Loudon, amounted to affirmative misconduct.

As part of this remedial scheme, the Customs Service is required under 19 C.F.R. §111.27 to audit the books and records of brokers. Significantly, this regulation incorporates the language of 19 U.S.C. §1641, by stating that audits *shall be made in order "to obtain information* regarding specific Customs transactions for the *purpose of protecting importers or the revenue of the United States."*[12]

The Customs Service, however, despite the adverse findings of the 1977 audit of Loudon and Loudon's presentation of at least six checks for Cometals' entries in one year, which were returned for insufficient

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[12] *Compare*, e.g., 19 C.F.R. 111.29 (1980), which provides in pertinent part:

> Each broker shall exercise due diligence in making financial settlements, in answering correspondence, and in preparing or assisting in the preparation and filing of documents relating to any matter handled by him as a broker. Funds received by a broker from a client for payment of duty, tax, or other debt or obligation owing to the Government shall be paid to the Government within 30 days from date of receipt or date due, whichever is later.

funds, failed to supervise Loudon in any way.[13] The Customs Service's violation of law caused importers, such as Cometals, relying on the Customs Service to fulfill its responsibility to supervise the activities of brokers, to continue to deal with Loudon to their detriment.

The government's affirmative misconduct in repeatedly violating its own law and regulations and in ignoring Congress' mandate by continuing to do business with Loudon after it knew for a period of three years that Loudon was insolvent and had mishandled importers' funds, gives rise to a finding of estoppel. As the court in *Corniel-Rodriguez v. I.N.S.*, 532 F.2d 301, 306 (2nd Cir. 1976) held, "[n]on compliance with an affirmatively required procedure, obviously designed to protect individuals . . . (is) an act of affirmative misconduct . . ." Under these circumstances, the Customs Service had a responsibility to monitor and possibly restrict the activities of Loudon.

The inevitable result of the Customs Service's misconduct—the inevitable result Congress sought to avoid in enacting the provisions governing customs brokers—was a loss to both Cometals and the Treasury. The Court of International Trade found that the Customs Service had no one to blame but itself for its failure to collect the $230,344.12 in import duties which Cometals tendered to Loudon, a finding not disturbed on appeal by the CAFC.

Permitting the decision of the CAFC to stand, a decision which essentially holds that the government

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[13] The CAFC never disturbed the Court of International Trade's finding that failure to supervise the broker in this case was affirmative misconduct.

can commit egregious violations of law and yet never be called to account for its actions leaves an injured citizen without a remedy and, furthermore, invites government misconduct. As the Court of International Trade correctly noted:

> . . . failing to estop the government when it has breached the law would encourage disobedience of the law by the government as well as private citizens. [Appendix C, at 39a].

Therefore, this Court should grant this petition in order to set out the limits of the defense of equitable estoppel, restore the holding of the Court of International Trade, and overrule the CAFC's *per se* rule.

III. The Petition Should Be Granted To Carry Out Congress' Intent To Permit Counterclaims Against The Government In Import Transactions.

In this case, the CAFC held that recoupment was unavailable to petitioners for the same reasons that equitable estoppel was unavailable. This holding, on an issue of nationwide applicability was incorrect and contrary to Congress' intent. This court should grant the petition in order to carry out that intent.

Recoupment is a common law doctrine which, unlike other counterclaims, does not request affirmative relief but operates only to defeat or modify a plaintiff's recovery on the main claim. Recoupment was formerly regarded as an affirmative defense, although it is now classified as a type of counterclaim under Rule 13 of the Federal Rules of Civil Procedure. *Frederick v. United States*, 386 F.2d 481, 487-488 (5th Cir. 1967).

The Court of International Trade, under the Custom Courts Act of 1980[14] was given the power to hear and adjudicate defendants' counterclaims by virtue of 28 U.S.C. §1583 which provides as follows:

> Sec. 1583. Counterclaims, Cross-claims, and Third party actions:
>
> In any civil action in the Court of International Trade, the court shall have exclusive jurisdiction to render judgment upon any counterclaim, cross-claim, or third-party action of any party, if (1) such claim or action involves the imported merchandise that is the subject matter of such civil action, or (2) such claim or action is to recover upon a bond or customs duties relating to such merchandise.

The counterclaim of recoupment involves the imported merchandise that is the subject of the government's suit.

In enacting the Customs Courts Act of 1980 Congress set out "to provide for a comprehensive system of judicial review of civil actions arising from import transactions, and to ensure the uniformity afforded by the national jurisdiction of these courts." *Customs Courts Act of 1979, S. 1654: Hearings on S. 1654 Before the Subcommittee on Improvements in Judicial Machinery*, Senate Committee on the Judiciary, 96th Cong. 1st Sess. (1979).

As originally drafted, the bill to expand the powers of the former Customs Court allowed only the government to counterclaim. The House of Representatives Report quoted the statement of the Chairman

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[14] *See* Pub.L. No. 96-417, 94 Stat. 1727 (1980).

of the ABA Standing Committee on Customs Law, that the widening of the right to counter or cross claim in an action brought by the Government

> . . . would contribute to the effectiveness of the judicial process, since it would permit the Court of International Trade to dispose of all claims arising out of the same underlying transaction in the one proceeding which it must conduct in any event. H.R. Rep. No. 96-1235, 96th Cong., 2d Sess. 37 (1980).

The present wording of Section 1583 was, therefore, proposed with the intent of giving defendants in a suit under Section 1582 the right to counterclaim against the government.[15]

The CAFC's holding, therefore, overturns Congress' scheme of comprehensive, nationwide resolution of Customs cases exclusively in the Court of International Trade. This Court should grant the petition in order to restore Congress' intent to resolve these issues of nationwide applicability in the Court of International Trade.

CONCLUSION

For the foregoing reasons, we respectfully submit that this petition for a writ of certiorari to the United States Court of Appeals for the Federal Circuit should be granted.

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[15] No other statutory waiver of sovereign immunity is necessary to give rise to a claim in recoupment. *Frederick v. United States, supra.*

Respectfully submitted,

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March 9, 1987

**Counsel of Record*

APPENDIX

APPENDIX A

United States Court of Appeals for the Federal Circuit

Appeal No. 85-2343

UNITED STATES,

Appellant,

v.

FEDERAL INSURANCE COMPANY and COMETALS, INC.,

Appellees.

Barbara M. Epstein, Commercial Litigation Branch, Department of Justice, of New York, New York, argued for appellant. With her on the brief were *Richard K. Willard*, Acting Assistant Attorney General, *David M. Cohen*, Director and *Joseph I. Liebman*, Attorney in Charge, International Trade Field Office.

David Serko, Serko, Simon & Abbey, of New York, New York, argued for appellee.

Appealed from: U.S. Court of International Trade

Judge Watson

United States Court of Appeals for the Federal Circuit

Appeal No. 85-2343

UNITED STATES,

Appellant,

v.

FEDERAL INSURANCE COMPANY and COMETALS, INC.,

Appellees.

DECIDED: November 10, 1986

Before MARKEY, *Chief Judge*, NIES and NEWMAN, *Circuit Judges*. NIES, *Circuit Judge*.

The United States appeals the judgment of the United States Court of International Trade in *United States v. Federal Insurance Co. and Cometals, Inc.*, 605 F. Supp. 298 (Ct. Int'l Trade 1985), holding that the government is equitably estopped from collecting certain import duties from an importer, Cometals, Inc., and its surety, Federal Insurance Company. Our jurisdiction over the appeal is found in 28 U.S.C. § 1295(a)(5). We reverse and remand with the direction to enter judgment for the government.

I.

This appeal raises the question of whether the government or an importer bears the risk of non-payment of import duties by a licensed broker who fails to pay over monies the broker received from the importer for payment of duties. On a theory of equitable estoppel the Court of

International Trade placed the risk on the government. We disagree. In sum, we reaffirm that a licensed broker is the agent of the importer, not of the government, and that no equitable estoppel can arise against the government in connection with an obligation to pay taxes. We further hold that, in any event, no basis for equitable estoppel exists in this case. Contrary to the trial court's holding, the government violated neither statute nor regulation in accepting an uncertified check from a broker which was secured by a bond given by the importer. The importer and his surety remain liable for duties owed to the government regardless of the malfeasance or misfeasance of a broker. Where the government is aware that a broker is in a precarious financial condition or has mishandled the affairs of importers, the government is obliged to investigate and, in appropriate circumstances, to suspend or revoke the license of such broker. However, the statutory provision regarding supervision of brokers for the protection of importers in *general* creates no right in an *individual* importer to be relieved of his outstanding tax obligations, indeed, is irrelevant to his continued liability.

Thus, the Court of International Trade erred, as a matter of law, in holding that the government was equitably estopped from collecting from the importer and its surety the duties owed to the public fisc.

II.

The United States, plaintiff below, brought suit in the United States Court of International Trade to recover unpaid liquidated import duties in the amount of $230,344.12, plus interest, against the importer, Cometals, Inc., and its surety on a bond, Federal Insurance Company.

On May 7, 1980, an entry had been filed at the Port of Los Angeles, California, showing Cometals as importer of record of 715 drums of titanium sponge being exported

from China by Japan. This entry had been made on behalf of Cometals by its customhouse broker, James Loudon & Co., Inc., which has since declared bankruptcy.

In connection with this entry, Cometals and Federal Insurance Co. had executed and delivered a general term bond to the Customs Service. Because the bond guaranteed payment of the duties, the imported merchandise was released to Cometals on the date entry was made, prior to the payment of duties. Cometals had, however, wired the amount of the import duties to Loudon's account on or about May 2, 1980. Loudon issued its own uncertified check in the amount of the estimated duties to the Customs Service on May 12, 1980.

The Customs Service accepted Loudon's uncertified check, asserting in this suit that acceptance of that check was required under Customs Regulation 19 C.F.R. § 24.1(3), which states that "an uncertified check drawn by an interested party . . . shall be accepted if there is on file . . . an entry bond or other bond to secure the payment of duties. . . ."[1]

When Loudon's check was not honored by its bank because of insufficient funds, the Customs Service obtained a second check from Loudon. However, this check was also not paid by the bank. After further attempts to secure payment from Loudon, the Customs Service then turned

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[1] 19 C.F.R. § 24.1(3) reads in pertinent part as follows:

§ 24.1 Collection of customs duties, taxes, and other charges.

• • •

(3) An uncertified check drawn by an interested party on a national or state bank or trust company of the United States or a bank in Puerto Rico or any possession of the United States if such checks are acceptable for deposit by a Federal Reserve bank, branch Federal Reserve bank, or other designated depositary shall be accepted if there is on file with the district director an entry bond or other bond to secure the payment of the duties, taxes, or other charges. . . .

to the importer and its surety for payment. Upon their refusal, the government instituted suit to collect the unpaid import duties from these parties. In response to the government's complaint, Cometals and its surety asserted "equitable estoppel" as an affirmative defense, as well as a number of counterclaims against the government.[2] Ruling on cross-motions for summary judgment, the trial court denied the government's motion and granted appellees' motion, holding that the United States was equitably estopped from recovering on its claim. 605 F. Supp. at 299.

The Court of International Trade based its holding essentially on the following determinations:

(1) As a matter of law, the United States can be equitably estopped from recovering import duties if it commits affirmative misconduct.

(2) The government committed affirmative misconduct in this case by accepting an uncertified check from a customhouse broker which was secured by the bond of the importer. Customs Regulation 19 C.F.R. § 24.1(3), which requires acceptance of an uncertified check which is secured by a bond, must be interpreted to require that the customhouse broker file its own bond to secure payment of the broker's uncertified check. The interpretation by the Customs Service of 19 C.F.R. § 24.1(3) is contrary (per the court) to congressional intent and to three statutory provisions: 19 U.S.C. § 66 (regulations must be consistent with law), 19 U.S.C. § 1641(d) (Secretary shall prescribe regulations for the licensing of brokers as he may deem necessary to protect importers and the revenue of the United States), and 19 U.S.C. § 1648 (Secretary

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[2] All of the counterclaims were dismissed for lack of jurisdiction with the exception of a claim for "equitable recoupment" which the court did not find necessary to decide in view of its upholding the defense of equitable estoppel. This counterclaim fails, *inter alia*, for the same reason as the defense of estoppel.

shall prescribe regulations for receiving uncertified checks in payment of duties).

(3) The government also committed affirmative misconduct by the "loose enforcement of 19 C.F.R. § 111.27," with respect to auditing of brokers, and by not following up on a 1977 audit of Loudon, which showed a "severe net worth deficiency."

The trial court noted in connection with the last point that Loudon's September 1977 financial statement, obtained as a result of an audit, showed that Loudon's liabilities exceeded its assets by over $164,000.00 and that Loudon had been responsible for more than $190,000.00 in overdrafts. In late 1979 and early 1980, six of Loudon's checks covering Cometals' entries were originally not paid by Loudon's bank because of insufficient funds, but all except the last, which was for the duties of this case, were paid on resubmission. Despite these warning signs since 1977, the government made no further audit of Loudon. It continued to accept Loudon's uncertified checks where the duties were guaranteed by a bond.

The trial court concluded that, in its view, the government "disregarded its own regulations, interpreted a decisive regulation unlawfully, and disregarded the manifest intention of Congress" and, thus, was equitably estopped from recovery on its claim. 605 F. Supp. at 299. The court acknowledged that "the opinion in *Air-Sea Brokers v. United States*, 66 C.C.P.A. 64, C.A.D. 1222, 596 F.2d 1008 (1979) held that equitable estoppel is not available in cases involving the collection of duties on imports." It distinguished *Air-Sea Brokers* from this case on the ground that the earlier decision did not involve the agency's breach of a regulation or statute, as did the case at hand, but rather "milder and more ambiguous" conduct by government employees. *Id.* at 304. The court also noted the decision of the Supreme Court in *Heckler v. Community Health Services of Crawford*, 104 S. Ct. 2218, 2224 (1984), which

implies that the government could be estopped although on a more stringent standard than a private litigant.

Relying on the violations it perceived, the court opined that the reasons for generally denying estoppel against the government could not justify the government's misconduct in failing to protect the importer and the public revenue. Thus, the suit by the government was not in the public interest. To uphold the government would encourage the government in its disobedience of the law. Under these circumstances, the government had "no right to resist the just effect of equitable estoppel." *Id.* at 305.

III.

In *Air-Sea Brokers*, the Court of Customs and Patent Appeals, a predecessor of this court whose decisions are binding precedent (*South Corp. v. United States*, 690 F.2d 1368, 1370-71, 215 USPQ 657, 657-58), held without equivocation:

> Accordingly, we hold that equitable estoppel, even if available in cases involving the Government in its proprietary capacity, is not available against the Government in cases involving the collection or refund of duties on imports.

596 F.2d at 1011. In reaching its decision, our predecessor relied on *Automobile Club of Michigan v. Commissioner*, 353 U.S. 180, 183 (1957) in which the Supreme Court stated, in connection with a tax claim, that "[t]he doctrine of equitable estoppel is not a bar to the correction by the Commissioner of a mistake of law."

Contrary to the analysis of the trial court, the decision in *Air-Sea Brokers* was not dependent on the "milder and more ambiguous" nature of the conduct of a particular government employee in contrast to the breach of the statute or regulation by the Secretary's wrongful interpretation of his authority. The case holds broadly that no

estoppel can arise against the sovereign act of tax collection and has been relied on and applied in other customs duties cases, *e.g.*, *United States v. Reliable Chemical Co.*, 605 F.2d 1179, 1184 (CCPA 1979). Even if this panel disagreed with that tenet, it is powerless to overturn it.

Nor are we inclined to recommend reconsideration of settled law by this court *in banc* in this case. If we assume that an equitable estoppel might be found in extraordinary circumstances, the holding by the trial court on equitable estoppel is based on an erroneous interpretation of the statute and regulations. There is no "illegal" conduct by the agency on which to predicate an estoppel in this case.

The trial court held that 19 C.F.R. § 24.1(3) (*supra*, note 1) must be interpreted to require that an uncertified check of a broker shall be accepted only if a bond has been posted *by the broker*. In the words of the trial court:

> The regulation in question, 19 C.F.R. § 24.1(3), must be interpreted so that it comports with the law, in which case, the bond posted *must* be the bond of the party making payment. Any interpretation of this regulation which would allow the bond of the importer to protect the legal obligation of the broker is unlawful.

605 F. Supp. at 302.

Only if the broker posts the bond, per the court, have the interests of the importer and the public revenue been protected as required by 19 U.S.C. § 1641(d). The Secretary, on the other hand, has taken the position, since at least 1955, that the government must accept an uncertified check if the bond *of any interested party* is posted covering the payment of the duties for which the check is tendered. As stated in the explanation of the amendment to section 24.1(3) which changed the language of the regulation to that which is under consideration:

> Section 24.1(3) now contains a provision that an uncertified check which can be cashed without expense to the Government shall be accepted by the collector of customs in payment of duties and other charges if drawn and tendered by a business or other organization, or by an individual, "who has on file with the collector of customs a customs entry bond or other bond to secure the payment of such duties or other charges." *It is [sic, was] not intended that this provision be interpreted as requiring that the drawer of the check and the principal on the bond shall necessarily be the same person or organization, and it is deemed desirable to clarify the regulation on this point.*

20 Fed. Reg. 8,775 (1955).

Thus, the interpretation which the trial court finds clearly illegal and contrary to congressional intent is one explicitly announced and consistently applied for more than 30 years.

We have no record here from which we might learn the advantages, as opposed to the disadvantages, to importers in having an importer -- as opposed to his broker -- post the bond. However, since no importer has previously challenged the government's interpretation, despite hundreds of thousands of entries, we can only surmise that the government's interpretation is not wholly unsatisfactory to the importing community. Nor has Congress undertaken to overrule the Secretary's interpretation despite numerous opportunities since 1955. "[C]ongressional failure to revise or repeal the agency's interpretation is persuasive evidence that the interpretation is the one intended by Congress." *NLRB v. Bell Aerospace Co.*, 416 U.S. 267, 275 (1974).

The foregoing historical facts were not taken into consideration by the trial court in holding that the Secretary's

interprettion of 19 C.F.R. § 24.1(3) was illegal. The function of a court is not, of course, to determine in this type of situation whether the Secretary's interpretation is the only possible interpretation of the statute, *Chemical Manufacturers Assoc. v. Natural Resources Defense Council, Inc.*, 105 S. Ct. 1102, 1108 (1985), but to determine whether the Secretary's interpretation is reasonable. As held in *Chevron U.S.A. Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837, 844 (1984), "[A] court may not substitute its own construction of a statutory provision for a resonable interpretation made by the administrator of an agency." Given the Secretary's long-standing and consistent interpretation, a court must be particularly circumspect in substituting its view of the statute for that of the agency charged with the responsibility for its administration. *See Young v. Community Nutrition Institute*, 106 S.Ct. 2360 (1986).

In holding that the Customs Service violated the statute in accepting the uncertified check of the broker not backed by the broker's own bond, as indicated, the trial court relied on three statutory provisions, which the court held were in *pari materia*, each of which grants the Secretary authority to issue certain regulations: 19 U.S.C. § 66, 19 U.S.C. § 1641(d) and 19 U.S.C. § 1648. Each of these provisions must be examined in turn.

Section 66

Section 66 is of no significance to the issue of whether the Secretary's interpretation of section 24.1(3) is legal or illegal. Section 66 provides simply that the Secretary shall prescribe rules and regulations with respect to import duties not inconsistent with law.[3]

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[3] 19 U.S.C. § 66 provides:

> The Secretary of the Treasury shall prescribe forms of entries, oaths, bonds, and other papers, and rules and regulations not in-

Section 1641

Section 1641 deals with the licensing of brokers. It provides, *inter alia*, that no one may act as a customhouse broker without a license, and for the Secretary to prescribe rules and regulations governing their licensing. Section 1641(b), which authorizes revocation or suspension of a broker's license upon notice, and a due process hearing, provides:

> [After notice and a hearing] the said Secretary of the Treasury shall have the right to revoke or suspend the license of any customhouse broker shown to be incompetent, disreputable, or who has refused to comply with the rules and regulations issued under this section, or who has, with intent to defraud, in any manner willfully and knowingly deceived, misled or threatened any importer, exporter, claimant or client, . . . by word, circular, letter or by advertisement.

Section 1641(d), which the trial court found was violated by the Secretary's interpretation of his regulation, reads as follows:

> (d) Regulations by Secretary. The Secretary of the Treasury *shall prescribe such rules and regulations as he may deem necessary to protect importers and the revenue of the United States*, and to carry out the provisions of this section, including rules and regulations requiring the keeping of books, accounts, and records by customhouse brokers, and the inspection thereof, and of their papers, documents, and correspond-

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consistent with law, to be used in carrying out the provisions of law relating to raising revenue from imports, or to duties on imports, or to warehousing, and shall give such directions to customs officers and prescribe such rules and forms to be observed by them as may be necessary for the proper execution of the law.

> ence by, and the furnishing by them of information relating to their business to, any duly accredited agent of the United States. (Emphasis added.)

In connection with enacting the comprehensive plan of section 1641 to regulate brokers, the legislative history contains the following expression of congressional intent:

> Although the great majority of these brokers are entirely above reproach in the conduct of their business, the corrupt practices of a few, unhampered by adequate statutory provisions for supervision, have proved a grave menace to importers and customs revenue alike. The present amendments are designed to remedy this situation. They will give to the Secretary of the Treasury the power to regulate the conduct of the business of customhouse brokers in such a manner that the opportunity for fraudulent practices will be reduced to an absolute minimum.

S. Rep. No. 1170, 74th Cong., 1st Sess. 3 (1935).

Section 1648

Section 1648 is not directed to brokers but rather deals with the subject of methods of payment of duties. In contrast to the authority of the Secretary in connection with other types of tax obligations, Congress has never allowed the Secretary to accept uncertified checks tendered in payment of import duties except under certain conditions. Section 1648 was enacted to liberalize the Secretary's authority, which had been more rigidly circumscribed, and reads in its entirety:

> Customs officers may receive uncertified checks, United States notes, and circulating notes of national banking associations in payment of duties on imports, during such time and under such rules

> and regulations as the Secretary of the Treasury shall prescribe but if a check so received is not paid the person by whom such check has been tendered shall remain liable for the payment of the duties and for all legal penalties and additions to the same extent as if such check had not been tendered.

The trial court held that the above authority of the Secretary with respect to regulating methods of payment was restricted by the requirement of section 1641, with respect to licensing brokers, that the Secretary *shall* issue regulations which protect importers. The mandatory language "*shall*" in section 1641(d) was controlling, per the trial court, with respect to the regulations under section 1648, and made the Secretary's interpretation of 19 C.F.R. § 24.1(3) issued under section 1648 illegal. We disagree that the Secretary's authority under section 1648 is so circumscribed.

While the trial court correctly noted the words of section 1648(d) [sic, 1641(d)] that the Secretary shall prescribe regulations to protect the importer, the court failed to take into account that the Secretary has been given wide discretion in deciding the scope of such regulations. Congress did not direct that the regulations must protect importers from all improvident or malicious acts of brokers. Rather it provided that the Secretary shall prescribe such regulations "as he may deem necessary to protect importers and the revenue of the United States." The words "as he may deem necessary" indicate that Congress intended to restrict judicial interference with the Secretary's exercise of his power. *See Young v. Community Nutrition Institute*, 106 S. Ct. at 2364-65.

The trial court also misconstrued the Congressional intent expressed in section 1641. Section 1641, in its entirety, does not require that the Secretary protect each importer from a particular financial loss or injury by a

particular broker. Section 1641 contemplates the withdrawal of licenses only *after* misconduct.[4]

Section 1641 imposes no obligation on the government to advise all importers or any particular importer that a particular broker is in a possibly shaky financial condition. Either a broker is licensed or he is not.[5]

As indicated in the legislative history, these statutory provisions are designed to protect the importing community by giving the Secretary the power to regulate the conduct of brokers and to reduce, thereby, the possibility of fraud to a minimum. The government, by granting a license and by having the power to withdraw that privilege, is not obligated to become the guarantor of each transaction conducted by a broker. Nothing in the legislative history leads to a contrary conclusion. Nor must the

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[4] Cometals argues that its broker, Loudon, was initially or became the agent of the government, and that Cometals' payment to the broker, therefore, constituted payment to the government. The theory that a broker is an agent of the government because the broker may operate only after obtaining a government license is again rejected. *See E.H. Carrigan v. United States*, 35 CCPA 10 (1947). The broker licensing program is designed to provide a substantial measure of protection to the public with whom brokers deal. But a broker is in a position no different from any other professional or skilled person who may legally operate only under a government license, for example, a registered patent attorney. The grant of such license represents to the public simply that certain minimum requirements necessary to practice their profession have been shown to be satisfied. It does not constitute a representation by the government that the broker will on all occasions properly handle the business of a client. Nor does misconduct somehow convert the broker to the agent of the government.

[5] It is inconceivable to the majority that the government could be held under an obligation to warn importers away from a broker who is licensed, or may publicly disclose a broker's financial condition. Section 1641(b) is designed to provide a large measure of protection for brokers. The suggestion that the government must warn prospective clients against a broker would circumvent these safeguards and must be unequivocally rejected.

Secretary provide in 19 C.F.R. § 24.1(3) that the broker must post his own bond for his uncertified check. Such a requirement would conflict with the flexible authority intended to be conferred by 19 U.S.C. § 1648.

The trial court mistakenly found support for its view in the following language of section 1648, "[I]f [an uncertified] check so received is not paid the person by whom such check has been tendered shall remain liable for the payment of the duties. . . ." The trial court reasoned that since the broker tendered the check, the broker remained liable and therefore, the broker's bond had to be on file to meet his obligation. The court erred, however, in its understanding of the meaning of this provision. The provision that the person tendering the check "shall remain liable" has no applicability to the broker. The broker was *never* liable to the government for the duties. Thus, under section 1648, the broker cannot "remain" liable for duties for which it was never liable.

The trial court also incorrectly concluded that if the regulation did not require that the bond be that of the broker, it "would allow the bond of the importer to protect the legal obligation of the broker. . . ." This analysis is backwards. It is the importer who has the legal obligation to the government to pay the duties, and the bond protects the legal obligation of the importer.[6] The trial court con-

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[6] This premise is clearly supported by 19 C.F.R. § 141.1(b) (1980) which states:

> (b) Personal debt of importer. The liability for duties, both regular and additional, attaching on importation constitutes a personal debt due from the importer to the United States which can be discharged only by payment in full of all duties legally accruing, unless relieved by law or regulation. It may be enforced notwithstanding the fact that an erroneous construction of law or regulation may have enabled the importer to pass his goods through the customhouse without such payment.

See also Meredith v. United States, 38 U.S. (13 Pet.) 486, 493 (1839)

fused obligations between the broker and the importer with obligations of the importer to the government.

In view of the above considerations, we hold that the Secretary's interpretation of 19 C.F.R. §24.1(3) is reasonable and that acceptance of Loudon's uncertified check in reliance on Cometals' bond was not a violation of the statute or the regulation.[7]

The basis for the trial court's holding on equitable estoppel being erroneous as a matter of law, the judgment cannot stand.

IV.

For the foregoing reasons, the judgment of the Court of International Trade holding that the government is equitably estopped from collecting duties owed by the importer Cometals and its surety is reversed. The case is remanded for entry of a judgment on liability in favor of the government and such further proceedings as are consistent with this opinion.

REVERSED AND REMANDED

(import duties constitute a personal debt due to the United States from the importer).

[7] The artificiality of this entire analysis based on 19 C.F.R § 24.1(3) is illustrated by the fact it can be raised in this case only because the broker issued his check. If the broker had not done so, the foundation for the argument simply disappears.

United States Court of Appeals for the Federal Circuit

Appeal No. 85-2343

UNITED STATES,

Appellant,

v.

FEDERAL INSURANCE COMPANY and COMETALS, INC.,

Appellees.

NEWMAN, *Circuit Judge*, dissenting.

I respectfully dissent.

In this case of neglect of duty by government agents in administering a statute enacted for the purpose of protecting importers and the United States against the notorious potential for abuse by customhouse brokers, the trial court had sound basis for invoking the doctrine of equitable estoppel. The majority's opinion pays scant deference to the facts as found by the Court of International Trade, none of which the majority finds to be clearly erroneous.

Appellate review of an equitable judgment requires not only attention to the specific abuses that led the court to impose an equitable remedy; but more, it requires appropriate deference to the discretionary authority with which trial judges are invested. Trial courts "in the framing of equitable decrees, are clothed 'with large discretion to model their judgments to fit the exigencies of the particular case.' " *United States v. E.I. du Pont de Nemours & Co.*, 353 U.S. 586, 607-08 (1956) (quoting *International Salt Co. v. United States*, 332 U.S. 392, 400-01 (1947)). *See also Curtiss-Wright Corp. v. General Electric Co.*, 446 U.S. 1, 10 (1980) ("the discretionary judgment of the district court

should be given substantial deference"). The basis for our review of the decision of the Court of International Trade is whether the court abused its discretion in imposing equitable estoppel, on the uncontested facts of this case. See *Albemarle Paper Co. v. Moody,* 422 U.S. 405, 424 (1975) in which, in directing the Fourth Circuit as to the standard to apply to the district court's determination of whether respondents were entitled to the equitable remedy of back-pay, the Supreme Court stated:

> [T]he standard of review will be a familiar one of whether the District Court was "clearly erroneous" in its factual findings and whether it "abused" its traditional discretion to locate "a just result" in light of the circumstances peculiar to the case . . . .

See also Los Angeles Department of Water & Power v. Manhart, 435 U.S. 702, 729 (1978) (Marshall, J., concurring in part and dissenting in part).

A trial court's exercise of equitable discretion based on specific circumstances is the acme of the judicial obligation to do justice under law. It is not defeasible by generalities as to the absolute right of the sovereign to extract monies from citizens -- a right that is not absolute, as this nation declared in 1776. The government is subject to minimal standards of responsibility in dealing with the public, whether the matter at issue is customs duties or any other impost on the public.

In holding the United States estopped, the trial court, expert in customs law, invoked the policy behind the law that the government had failed to administer. The trial court declined to excuse the government from the consequences of this failure. Viewed another way, the trial court refused to penalize the innocent importer by requiring the importer to pay the duty of $230,334.12 twice, when governmental lapse was a significant factor in the event.

The trial court recognized, as had Congress when the current law controlling customs brokers was enacted, the unusual role of customhouse brokers in the customs business:

> [I]n view of the fact that these customhouse brokers are quasi-officers of the Treasury and that by licensing them the Treasury holds out to importers that it has investigated their character and represents to such importers that they are capable and honest in their conduct of their customs business . . . .

Cong. Rec. 13,356-57 (1935) (statement of Senator Walsh). *See also* S. Rep. No. 1170, 74th Cong., 1st Sess. 3 (1935).

As the trial court remarked, Loudon's history of bad checks and negative net worth was well known to the Customs Service. The legislative history shows that the regulation of customs brokers was designed to protect "both importers and the revenue of the United States". Cong. Rec. 13,387 (1935). Congressman Crowther reiterated that customs brokers are

> pseudo Federal officers in the sense that they handle the customs revenue as between the Government and the importer . . .

Cong. Rec. 14,577 (1935), and that in light of their "peculiar relation" to the federal government, the Treasury Department

> ought to have complete authority for a thorough examination of their transactions in order to end this racketeering and depleting of the revenue of the Government of the United States.

Id. This authority was enacted by statute:

> *Regulations by Secretary*
>
> The Secretary of the Treasury shall prescribe

> such rules and regulations as he may deem necessary *to protect importers and the revenue of the United States*, and to carry out the provisions of this section, including rules and regulations requiring the keeping of books, accounts, and records by customhouse brokers, and the inspection thereof. . . . [Emphasis added]

19 U.S.C. §1641(d).

Pursuant to this authority the Treasury examined Loudon's finances. A government audit in October 1977 revealed that Loudon's liabilities exceeded his assets by over $164,000, and that he was responsible for more than $190,000 in overdrafts. This in itself violated the standards for licensed brokers. In late 1979 and early 1980 six of Loudon's uncertified checks, some covering Cometals' entries, were dishonored and returned to the Customs Service on the basis of insufficient funds. The Customs Service never advised the importer of these events. Although Loudon eventually covered these checks, the government's blind eye to Loudon's style was inimical to its statutory responsibility.

Despite its knowledge of Loudon's negative net worth and its experiences with Loudon's bad checks, the Customs Service conducted no audit after 1977 of Loudon's financial condition, took no action in connection with Loudon's license, required no bond from Loudon, and did not tell the importer when its broker's checks were dishonored. Nothing whatsoever was done to protect either the importer or the United States, as required by statute. The trial court held that the government was equitably estopped, by these actions, from recourse against Cometals in this case.

Despite long-standing congressional and judicial recognition of the pragmatic role of customhouse brokers as "quasi-officers of the Treasury", the majority erases this history by its fiat that Loudon was a "mere agent" of the

importer. The past is not so easily changed. Indeed, the term "broker" itself connotes other than a simple agency relationship.

The trial court discussed its reasons for holding that customs brokers are not simply agents of the importer. But even on agency principles, the Customs Service failed in its obligations to the "principal" it now seeks to hold liable. The Customs Service never notified Cometals of its purported agent's bounced checks, neither in this case nor in prior importations where Loudon's checks for Cometals' duties were not honored.

> Third party disclosure to an agent is not imputed to the principal when the agent is acting adversely to the principal's interest and the third party has notice of this.

Arlinghaus v. Ritenour, 622 F.2d 629, 636 (2d Cir.), *cert. denied*, 449 U.S. 1013 (1980). *See also* Restatement (Second) of Agency § 271 (1958). The detrimental reliance element of estoppel, *e.g., Heckler v. Community Health Services, Inc.*, 467 U.S. 51, 59 (1984), was exacerbated by this silence. Further, any agency relationship between Loudon and Cometals vanished when Loudon comingled funds and diverted payments:

> [T]he authority of an agent terminates if, without knowledge of the principal, he acquires adverse interests or is otherwise guilty of a serious breach of loyalty to the principal.

Restatement, *supra*, § 112. The government knew of these adverse interests, and has not denied its knowledge of Loudon's financial practices. By the government's admissions, any agency authority was terminated by its and Loudon's actions adverse to Cometals' interest.

Cometals argued before the trial court that the Customs Service, in its tolerance of Loudon's misfeasances and in its failure to notify Cometals when the checks for Com-

etals' duties were dishonored, acted in a way that protected Loudon while prejudicing the importer. The government concedes in its brief that "there is no evidence on the record that the importer or surety were even aware that uncertified checks were being accepted". Loudon's bankruptcy ended a pattern of what Cometals describes as "kiting", facilitated by governmental violation of its own regulations.

The trial court was entitled to consider these circumstances in reaching its equitable decision. They can not be glossed over. The government argues that it was entitled to continue to process Loudon's succession of bad checks without advising the importer, even as it now seeks to hold the importer responsible for this clearly preventable occurrence.

The government argues that it accepted Loudon's uncertified check in this case because of Cometals' surety bond, but this is a different issue. I do not see how the presence of Cometals' bond is a sufficient excuse for the government's laxness, if not acquiescence, in Loudon's financial footwork when the Treasury regulations require the government to license only financially sound customs brokers. In view of the government's failure to meet its minimal regulatory obligations, it can not now argue that the statute

> 19 U.S.C. § 1648 . . . [I]f a check so received is not paid the person by whom such check has been tendered shall remain liable for the payment of the duties . . .

means not only the maker who tenders the check but the importer as well. The plain language of the statute excludes so expansive a reading. The statute itself accommodates the ever-present customs broker, and his complex relationship in such transactions.

Cometals' surety company bonded Cometals, not Loudon. The majority interprets Cometals' bond as Cometals'

surety's acceptance of liability to the government for Loudon's diversion of the monies. The majority holds that because of the bond the government had no obligation to enforce its own regulations, or even to exercise minimal due care in its dealings with Loudon and particularly in its dealings with importers. The Court of International Trade held that the Customs Service was chargeable with "affirmative misconduct" in not requiring a bond of Loudon and in failing to audit and determine his financial responsibility, as the law and Treasury regulations require. On this record, the imposition of equitable estoppel is supported by precedent.

Equitable estoppel against the government is imposed only in egregious circumstances, wherein to hold otherwise is offensive to one's sense of justice. The Supreme Court in *Heckler v. Community Health Services, Inc.*, 467 U.S. 51, 60-61 (1984), concluded that it would not

> say that there are *no cases* in which the public interest in ensuring that the Government can enforce the law free from estoppel might be outweighed by the countervailing interest of citizens in some *minimum standard of decency, honor and reliability* in their dealings with their Government. [Emphasis in original and added]

The Court in *Community Health Services* discussed various examples of governmental misconduct in which equitable estoppel was denied or granted depending on the facts, including *Immigration and Naturalization Service v. Miranda*, 459 U.S. 14, 17, 19 (1982) ("The Court of Appeals thus correctly considered whether as an initial matter, there was a showing of affirmative misconduct."); *Schweiker v. Hansen*, 450 U.S. 785, 788 (1981) (" 'It is the duty of all courts to observe the conditions defined by Congress for charging the public treasury.' ") (quoting *Federal Crop Insurance Corp. v. Merrill*, 332 U.S. 380, 385 (1947)). 467 U.S. at 60 n.12.

The Court in *Community Health Services* stated that "at least two of our cases seem to rest on the premise that when the Government acts in misleading ways, it may not enforce the law if to do so would harm a private party as a result of government deception." *Id.* (citing *United States v. Pennsylvania Industrial Chemical Corp.*, 411 U.S. 655, 675 (1973) (evidence of misleading information by government is pertinent to defense of whether it was reasonable to rely thereon); and *Moser v. United States*, 341 U.S. 41, 47 (1951) (finding "misleading circumstances" the Court held that "elementary fairness" required estoppel)).

There are varied circumstances in which equitable estoppel has been imposed by the courts against the government. Among the circuits, see, *e.g.*, *Meister Brothers, Inc. v. Macy*, 674 F.2d 1174, 1177 (7th Cir. 1982) ("the 'public has an interest in seeing its government deal carefully, honestly and fairly with its citizens' ") (quoting *United States v. Wharton*, 514 F.2d 406, 412-13 (9th Cir. 1975); *Corniel-Rodriguez v. Immigration and Naturalization Service*, 532 F.2d 301, 307 (2d Cir. 1976) (refusing "to sanction a manifest injustice occasioned by the Government's own failures"); *United States v. Lazy FC Ranch*, 481 F.2d 985, 989 (9th Cir. 1973) ("estoppel is available as a defense against the government if the government's wrongful conduct threatens to work a serious injustice and if the public's interest would not be unduly damaged by the imposition of estoppel"); *Brandt v. Hickel*, 427 F.2d 53, 56 (9th Cir. 1970) ("some forms of erroneous advice are so closely connected to the basic fairness of the administrative decision making process that the government may be estopped"); *United States v. Georgia-Pacific Co.*, 421 F.2d 92, 103 (9th Cir. 1970) ("the dictates of both morals and justice indicate that the Government is not entitled to immunity from equitable estoppel in this case"). The Court of Claims has held similarly, see *Emeco Industries, Inc. v. United States*, 485 F.2d 652, 657 (Ct. Cl. 1973) (government not immune from estoppel where its

denial would be " 'contrary to equity and good conscience' ") (quoting *Stevens Manufacturing Co. v. United States*, 8 F. Supp. 720, 724, 80 Ct. Cl. 183, 192-93 (1934)).

In *Air-Sea Brokers, Inc. v. United States*, 596 F.2d 1008 (CCPA 1979), the Court of Customs and Patent Appeals stated that equitable estoppel could not be applied against the government in cases involving import duties, based on its view of the distinction between governmental action in a sovereign capacity as opposed to a proprietary capacity, *id.* at 1011, a distinction inapt in the case at bar, as illustrated in the CCPA's reference to *Automobile Club v. Commissioner*, 353 U.S. 180, 183 (1957), a tax case which held that the Commissioner was not estopped from correcting an error of law and thereby requiring payment of past taxes, *id.* at 1101 n.8. In neither *Air-Sea Brokers* nor *Automobile Club* did the trial court find that there was affirmative misconduct; nor did the trial court in either case, in its equitable discretion, determine that the facts of the case warranted the application of the doctrine of equitable estoppel. Appropriately in view of the limited standard of review with respect to such issues, see discussion *ante*, each appellate court and in *Automobile Club* the Supreme Court affirmed. Therefore, unlike the situation now before us, in *Air-Sea Brokers* and *Automobile Club*, imposts were required to be paid rather than waived in their entirety. The case of *United States v. Reliable Chemical Co.*, 605 F.2d 1179 (CCPA 1979), relied on by the majority, does not relate to the collection of duties, but to the *jurisdictional* issue of the filing of a protest before instead of after liquidation.

The Court of International Trade thus declined to apply the CCPA's sweeping dictum, stating correctly that its holding does not "sanction *all* possible government misconduct in the area of duty collection, particularly when it displays a blatant disregard for the public interest in a matter of utmost importance." 605 F. Supp. at 304 (emphasis in original).

As is made clear in the extensive precedent in which courts have considered governmental conduct, whether the government can be estopped depends on the nature of both the governmental action and the governmental misconduct. The trial court referred to the general rule that " 'laches or neglect of duty on the part of officers of the Government is no defense to a suit by it to enforce a public right or protect a public interest' ", 605 F. Supp. at 303-04 (quoting *Utah Power & Light Co. v. United States,* 243 U.S. 389, 409 (1917)), a rule tempered by judicial determination of whether the government met a "minimum standard of decency, honor, and reliability", in the words of *Community Health Services.* In balancing these factors, the courts are obliged to administer laws fairly, even when the government is a party. Neither the government nor its citizens is relieved from the omnipresent obligation to "turn square corners" with the other. *St. Regis Paper Co. v. United States,* 368 U.S. 208, 229 (1961) (Black, J., dissenting), *quoted in Community Health Services,* 467 U.S. at 51 n.13; *Federal Crop Insurance Corp. v. Merrill,* 332 U.S. 380, 387-88 (1947) (Jackson, J., dissenting).

Equitable estoppel is not legal estoppel: it is the fruit of the search for justice in an often complex balance of interests, rights, and authorities. The laws requiring federal regulation of customhouse brokers were designed to protect both importers and the treasury, as is clear from the legislative history. Balancing the equities as between these two entities with respect to the circumstances at bar, the Court of International Trade brought its wisdom and experience in customs law and practice. None of the decisions cited by the government or relied on by the majority is contravened by the trial court's conclusion in this case. The decision of the Court of International Trade is supported by law and precedent and is in the interest of justice.

The Treasury changed its regulations in 1982, by requiring customs brokers to advise importers in writing that

importers may pay customs duties directly to the United States rather than to the broker, and that payment to the broker does not relieve the importer of liability. 19 C.F.R. § 111.29(b)(1). This change reinforces the view that the prior regulations and practices were notably imperfect. The trial court's decision is not contrary to law nor an abuse of its equitable discretion, and should not be disturbed.

APPENDIX B

United States Court of Appeals for the Federal Circuit

Appeal No. 85-2343

UNITED STATES,

Appellant,

v.

FEDERAL INSURANCE COMPANY and COMETALS, INC.,

Appellees.

ORDER

A suggestion for rehearing in banc having been filed in this case,

UPON CONSIDERATION THEREOF, it is

ORDERED that the suggestion for rehearing in banc is declined.

/s/ FRANCIS X. GINDHART
FRANCIS X. GINDHART, Clerk

12/8/86
Date

cc: Mr. David Serko
Ms. Barbara M. Epstein, New York City, DOJ

APPENDIX C

Slip Op. 85-32

UNITED STATES COURT OF INTERNATIONAL TRADE

Before WATSON, Judge

Court No. 82-05-00594

UNITED STATES OF AMERICA,

Plaintiff,

v.

FEDERAL INSURANCE COMPANY and COMETALS, INC.,

Defendants.

Action for Customs Duties—Equitable Estoppel

In an action by the government to collect customs duties from the importer and its surety the Court holds that the government is equitably estopped from making its claim because of its affirmative misconduct.

(Decided March 14, 1985)

Richard K. Willard, Acting Assistant Attorney General (*Joseph I. Liebman,* Attorney in Charge, International Trade Field Office and *Barbara M. Epstein,* Department of Justice, Civil Division Commercial Litigation Branch) for the plaintiff.

Serko & Simon (*David Serko, Margaret H. Sachter,* and *George S. Locker,* attorneys) for the defendants.

WATSON, Judge: The plaintiff brought this action against the importer, (Cometals, Inc.), and the importer's surety, Federal Insurance Company, in order to recover

approximately $230,344.12 in import duties, plus interest. It is before the court on the plaintiff's motion for summary judgment, defendants' opposition thereto and their cross motion for summary judgment on their counterclaims for equitable recoupment.[1] There is no dispute as to the facts.

Underlying this action is the plaintiff's failure to obtain payment of import duties, despite Cometal's transmittal of the money owed, to its broker, James Loudon & Co. (Loudon).

In this decision, the Court finds that the plaintiff-government disregarded its own regulations, interpreted a decisive regulation unlawfully, and disregarded the manifest intention of Congress. Thus, sole responsibility for not receiving the duties that are claimed to be owed by the defendants, must be attributed to the plaintiff's malfeasance. In short, the government is equitably estopped from recovering on its claim.

This action has its origin in the importation by Cometals of titanium sponge. As a result of the entry involved Cometals owed approximately $230,344.12 in import duties. Loudon, after receiving the necessary funds from Cometals on or about May 2, 1980, tendered its own *uncertified* check in the amount of $230,344.12 on May 12, 1980, as payment to the Customs Service for the duties owed by defendant-importer.

On May 29, 1980, however, this check was returned to Customs by the Bank of America because of insufficient funds in Loudon's account. Customs then requested and subsequently received a second check from Loudon on June 12, 1980. This check was also returned by the bank be-

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[1] In an earlier decision the Court dismissed counterclaims made by defendants under the Federal Tort Claims Act (28 U.S.C. §2671 et seq.), the Tucker Act (28 U.S.C. §1491), and the Administrative Procedure Act, 5 U.S.C. §701 et seq., *United States v. Federal Ins. Co. and Cometals Inc.*, 6 C.I.T. ___, (Slip Op. 83-118, November 15, 1983).

cause of insufficient funds. Finally, after the Customs Service's direct demands for payment from Loudon proved futile, it turned to the defendants for payment.

It should also be noted that the government had audited Loudon in October of 1977, and that audit had revealed a severe net worth deficiency. The September, 1977, financial statement, which the government admits it obtained as a result of this audit, showed that Loudon's liabilities exceeded its assets by over $164,000 and that it was responsible for more than $190,000 in overdrafts. Despite this fact, no further audits were conducted by the Customs Service.

Moreover, in late 1979, and early 1980, six of Loudon's uncertified checks covering Cometal's entries were returned to the government because of insufficient funds.[2] Nevertheless, the government continued to re-deposit those checks or to accept new checks from Loudon.

I.

Regulations promulgated by the Customs Service provide a detailed procedure for the payment of duties. *See generally,* 19 C.F.R. §24. The tender and acceptance of uncertified checks is governed by 19 C.F.R. §24.1(3) which reads as follows:

> 19 C.F.R. §24.1(3)
>
> (3) *An uncertified check drawn by an interested party* on a national or state bank or trust company of the United States or a bank in Puerto Rico or any possession of the United States if such checks are acceptable for deposit by a Federal Reserve bank, branch Federal Reserve bank,

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[2] For example, Check No. 43896 dated March 7, 1980, was not paid until April 21, 1980; Check No. 44314 dated April 15, 1980, was not paid until May 5, 1980.

> or other designated depository *shall be accepted if there is on file* with the district director *an entry bond or other bond* to secure the payment of the duties, taxes, or other charges, *or if a bond has not been filed, the organization or individual drawing and tendering the uncertified check has been approved by the district director to make payment in such manner.* In determining whether an uncertified check shall be accepted in the absence of a bond, the district director shall use available credit data obtainable without cost to the Government, such as that furnished by banks, local business firms, better business bureaus, or local credit exchanges, sufficient to satisfy him of the credit standing or reliability of the drawer of the check. [emphasis supplied]

The government argues that when it accepted the uncertified checks in question from Loudon it was acting in compliance with 19 C.F.R. §24.1(3). According to the government, as long as there was a bond on file, *even if it was a bond posted by the importer,* it was acting in accordance with the law.

The Court finds that the government's interpretation of 19 C.F.R. §24.1(3) violates three sections of the law which are in *pari materia;* 19 U.S.C. §66, 19 U.S.C. §1641(d) and 19 U.S.C. §1648.

19 U.S.C. §66 requires that all regulations prescribed by the Secretary of the Treasury relating to the collection of duties from importation must *not* be inconsistent with the law.

> §66. Rules and forms prescribed by Secretary
>
> The Secretary of the Treasury shall prescribe forms of entries, oaths, bonds, and other papers, and rules and regulations *not inconsistent with law,* to be used in carrying out the provisions of

> law relating to raising revenue from imports, or to warehousing, and shall give such directions to customs officers and prescribe such rules and forms to be observed by them as may be necessary for the proper execution of the law. [emphasis supplied]

19 U.S.C. §1641 deals with the regulation of brokers. When enacting 19 U.S.C. §1641(d) Congress expressly stated that the Secretary of the Treasury *shall* promulgate rules and regulations regarding Customs brokers to protect *both importers and the revenue of the United States.* 19 U.S.C. §1641(d) reads as follows:

> 19 U.S.C. §1641 Customhouse brokers
>
> (d) **Regulations by Secretary.** The Secretary of the Treasury *shall* prescribe such rules and regulations *as he may deem necessary to protect importers and the revenue of the United States,* and to carry out the provisions of this section, including rules and regulations requiring the keeping of books, accounts, and records by customhouse brokers, and the inspection thereof, and of their papers, documents, and correspondence by, and the furnishing by them of information relating to their business to, any duly accredited agent of the United States. [emphasis supplied]

This Court deems the word "shall" contained within 19 U.S.C. §1641(d) to be imperative in nature. Although Congress gave the Secretary certain discretion in how he promulgates regulations concerning the relationship between brokers, importers and the revenue of the United States, this Court finds that the Secretary *must,* when promulgating such regulations, adhere to Congress' directive that these regulations protect *both* the importers and the revenue of the United States.

If there remained any doubt as to why Congress used the word "shall" in 19 U.S.C. §1641(d), the legislative history of the 1935 amendment to 19 U.S.C. §1641(d) that added the language "to protect importers," makes it clear that Congress intended that the word "shall" be given its common imperative meaning. The overwhelming impact of this legislative history justified the following extended quotation:

> While the large importers are more or less familiar with customs procedure the great majority of importers are solely dependent upon the honesty and the competency of their customs brokers to protect their interests. Even in the case of large importers, however, due to the specialized nature of customs procedure, great reliance must be placed upon their brokers for proper entry of merchandise.
>
> In view of the fact that these customhouse brokers are quasi officers of the Treasury and that by licensing them the Treasury holds out to importers that it has investigated their character and represents to such importers that they are capable and honest in their conduct of their customs business, and in view of the large opportunities for profitable fraud open to dishonest persons who, from the very nature of things, occasionally succeed in obtaining licenses as customhouse brokers despite the strictest possible investigation by the Treasury of their character and qualifications, it is essential that the Department have wide discretion in dealing with these brokers and that the Secretary of the Treasury, therefore, be given broad powers to supervise and regulate their activities. Under existing law his powers in these respects are very limited, and it is the purpose of the present amendments to broaden the Secretary's powers

> so that he can in the future more effectively cope with frauds practiced by customhouse brokers on both importers and the revenues of the United States.
>
> Although the great majority of these brokers are entirely above reproach in the conduct of their business, the corrupt practices of a few, unhampered by adequate statutory provisions for supervision, have proved a grave menace to importers and customs revenue alike. The present amendments are designed to remedy this situation. They will give to the Secretary of the Treasury the power to regulate the conduct of the business of customhouse brokers in such a manner that *the opportunity for fraudulent practices will be reduced to an absolute minimum.* [emphasis supplied]

S. Rep. No. 1170, 74th Cong., 1st Sess., 3 (1935).

It is thus clear that Congress was extremely concerned with the victimization of importers by brokers and required that the Secretary prescribe regulations protecting both importers and the revenue of the United States from possible frauds by brokers.

19 U.S.C. §1648[3] granted the Customs Service broad authority to promulgate regulations regarding the payment of Customs duties with uncertified checks. *See* 19 C.F.R.

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[3] §1648. **Uncertified checks, United States notes, and national bank notes receivable for customs duties.**

> Customs officers may receive uncertified checks, United States notes, and circulating notes of national banking associations in payment of duties on imports, during such time and under such rules and regulations as the Secretary of the Treasury shall prescribe; *but if a check so received is not paid the person by whom such check has been tendered shall remain liable* for the payment of the duties and for all legal penalties and additions to the same extent as if such check had not been tendered. [emphasis supplied]

§24.1(3). However, when the Customs Service agrees to accept an uncertified check from a broker pursuant to any regulation it promulgates under 19 U.S.C. §1648, such regulation and the Customs Service's interpretation of this regulation, must conform to clear Congressional intent contained within 19 U.S.C. §1641(d).[4]

The regulation contained in 19 C.F.R. §24.1(3) cannot operate to the detriment of importers entrusting their funds to brokers, without violating 19 U.S.C. §1641(d). A regulation such as this one that authorizes the government to accept an uncertified check from a broker cannot be exclusively used for the protection of the revenue of the United States at the unwitting expense of the importer, without failing to fully effectuate 19 U.S.C. §1641(d) and its clear legislative purpose. It would be palpably absurd to have the importer guarantee the conduct of its broker when the clear intent of 19 U.S.C. §1641(d) was to protect *both* the revenue of the United States and the *importer* from possible misconduct by brokers.

It is inconceivable that the sum at issue would not be safely within the hands of the government, had it complied with its own regulation. The regulation in question, 19 C.F.R. §24.1(3), must be interpreted so that it comports with the law, in which case, the bond posted *must* be the bond of the party making payment. Any interpretation of this regulation which would allow the bond of the importer to protect the legal obligation of the broker is unlawful.

This Court also takes note of another regulation promulgated pursuant to 19 U.S.C. §1641 which also must protect *both* the importer and the revenue of the United States.

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[4] The regulation also expressly states that "[i]f a check so received is not paid *the person by whom such check has been tendered* shall remain liable for the payment of the duties. . . ." *See* 19 U.S.C. §1648. [emphasis supplied]

19 C.F.R. §111.27 states:

> The Regional Director . . . *shall* make such audit or inspection of the books and papers to be required to be kept and maintained by a broker as may be necessary . . . *to determine* whether or not the broker is complying with the requirements of this part. Furthermore the Regional Director . . . may inspect such books and papers to obtain information regarding specific Customs transactions for the purpose of *protecting importers* or the revenue of the United States. [emphasis supplied]

The Regional Director must conduct audits in a manner designed to protect both importers and the revenue of the United States. This Court cannot permit the plaintiff to benefit from its own violation of the law nor can it condone the Custom Service's failure to conform to its own regulations. By continuing to redeposit Loudon's "bouncing checks" in early 1980, the government was directly responsible for endangering the payment of duties by Cometals. At the same time, the government was not enforcing a law intended to protect *both* importers and the revenue of the United States.

The government's failure to act in accordance with 19 C.F.R. §24.1(3) and its violation of the manifest intention of Congress would be sufficient by itself to estop it from obtaining the duties in question. Moreover, by the loose enforcement of 19 C.F.R. §111.27 and by failing to follow up its September, 1977, audit of Loudon, the government was increasing its risk and the risk of importers who were entrusting their funds to the broker. This Court holds that under the facts presented the government has committed affirmative misconduct and further holds that it is equitably estopped from recovering the import duties in question.

II.

Equitable estoppel adjusts the relative rights of parties based upon a consideration of justice and good conscience. *United States v. Georgia-Pacific Company,* 421 F.2d 92, 95 (9th Cir. 1970) (and cases cited therein). It has been stated that equitable estoppel precludes a party both at law and equity "[f]rom asserting rights which might perhaps have otherwise existed either of property, of contract, or of remedy as against another person, who has in good faith relied upon such conduct, and has been led thereby to change his position for the worse, and who on his part acquires some corresponding right, either of property, of contract or of remedy." 3 Pomeroy, Equity Jurisprudence §804 at 189 (5th ed. Symons 1941).

Generally, in suits not involving the government, four elements must be present in order to establish the defense of estoppel: (1) the party to be estopped must know the facts; (2) he must intend that his conduct shall be acted on or must so act that the party asserting the estoppel has a right to believe it is so intended; (3) the latter must be ignorant of the true facts and (4) he must rely on the former's conduct to his injury, *United States v. Ruby Co.,* 588 F.2d 697, 703 (9th Cir. 1978).

The traditional elements of estoppel are clearly present in the instant action. The government knew about Loudon's precarious financial condition and improperly relied upon Cometal's bond when it accepted Loudon's uncertified checks. The defendants were not aware of Loudon's precarious financial condition, nor did they know that the government was relying on them as guarantors of Loudon's "bouncing" checks. The government's mechanism for collecting duties is in its nature intended to encourage reliance on its regularity and propriety by those owing duties. As a result of reliance on the propriety of the government's conduct, Cometals lost $230,344.12. The government's failure to adhere to its own regulations and to

act in accordance with the law provides the crucial element of affirmative misconduct that is necessary to estop the government.

The Court in *Corniel Rodriguez v. I.N.S.*, 532 F.2d 301 (2d Cir. 1976) held that: "[n]on compliance with an affirmatively required procedure, obviously designed to protect individuals . . . (is) an act of *affirmative misconduct*. . . . Indeed since 22 C.F.R. §42.122(d) was validly adopted . . . it carries the force of law (and) must be respected and enforced by the Government." *Corniel Rodriguez v. I.N.S.*, 532 F.2d, at 306, 307 (1976) (and cases cited therein). [emphasis supplied]

The presence of an additional element of affirmative misconduct must be established in order for the government to be subject to equitable estoppel. This additional element is necessary because the government cannot be estopped under the same terms as a private litigant:

> [W]hen the government is unable to enforce the law because the conduct of its agents has given rise to an estoppel, the interests of the citizenry as a whole in obedience to the rule of law is undermined. It is for this reason that it is well settled that the government may not be estopped on the same terms as any other litigant. *Heckler v. Community Health Services of Crawford*, ___ U.S. ___, 104 S. Ct. 2218, 2224, (1984).

This Court must take note however, that failing to estop the government when it has breached the law would encourage disobedience of the law by the government as well as private citizens.

It has also been said that the government cannot be estopped under the same conditions as a private party because of the government's responsibility to protect the

public interest.[5] "As a general rule, laches or neglect of duty on the part of officers of the Government is no defense to a suit by it to *enforce a public right or protect a public interest. . . . "Utah Power and Light Co. v. United States,* at 243 U.S. 389, 409 (1917) [emphasis supplied].

In the instant case the public interest required to be protected consisted of both the revenue of the United States and *importers.* The plaintiff here failed to comply with the law and ignored the public interest by not protecting *both* importers *and* the revenue of the United States. The reasons for limiting the application of equitable estoppel against the government certainly cannot justify the plaintiff's failure to act in accordance with the law in a matter of the utmost importance.

It must be acknowledged that the opinion in *Air Sea Brokers v. United States,* 66 C.C.P.A. 64, C.A.D. 1222, 596 F. 2d 1008 (1979) held that equitable estoppel is not available in cases involving the collection of duties on imports. The conduct complained of in *Air Sea Brokers* however, did not involve the breach of a regulation or a statute. In *Air Sea Brokers,* the alleged misconduct consisted of the filling out of forms by the government which might have allowed a broker to achieve duty free entry without certain documents. This conduct was counterbalanced by an ambiguous stamp on the form and more importantly, actual knowledge by the broker that the Custom Service was not waiving the documentary requirement.

Thus, the government's conduct in *Air Sea Brokers* was milder and more ambiguous than the conduct involved in

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[5] The sovereign's duty to protect the public interest is subsumed within the doctrine of sovereign immunity. However the scope of sovereign immunity and the degree to which it has insulated the government has been narrowed considerably. The doctrine of sovereign immunity and its corollary the governmental-proprietary distinction has been criticized and narrowed. See *United States v. Georgia Pacific Co.,* 421 F.2d 92, 99. *See also Garcia v. San Antonio Metropolitan Transit Authority,* 53 U.S.L.W. 4135, 4137-4140 (U.S. Feb. 19, 1985).

this case. In the instant case there is no possible ambiguity in what the government did and no ameliorating factors in justifying its dereliction of duty. Here, the conduct of the government directly contravened two basic purposes of the law; the protection of the revenue of the United States and the protection of importers. Also of significance is that in the instant action, the defendants justifiably relied on the government's conformance with the law, while in *Air Sea Brokers,* the broker had actual knowledge of the government's conduct. The opinion in *Air Sea Brokers* does not to sanction *all* possible government misconduct in the area of duty collection, particularly when it displays a blatant disregard for the public interest in a matter of the utmost importance.

Moreover, for the government to be immune from the defense of equitable estoppel it must be acting for the benefit of the public. *See Utah Power and Light v. United States, supra.* Thus, in *Federal Crop Insurance v. Merrill,* 332 U.S. 380 (1947) a farmer who had planted wheat relying on the advice of an agent of the Federal Crop Insurance Corp. (FCIC) that it was insured under its program could not recover for the loss of his crop, because the regulation of the FCIC precluded coverage for spring wheat which had been reseeded on winter wheat acreage. To permit the farmer to recover in *Federal* would undermine a fundamental public policy.

In the instant case it is affirmative *government conduct* not the representation of a mere government agent that has contravened the government's own regulations as well as the express intent of Congress. Here, it is the government that has acted in opposition to the public interest, by violating its duty to protect both importers and its own revenue. The government has given a higher priority to a display of leniency to a broker, the one party under the facts presented whose role is least identifiable with the public interest. The violation of the government's duty to

protect importers as well as the revenue of the United States cannot be sanctioned by this Court.

In *I.N.S. v. Miranda,* 459 U.S. 14 (1982) an 18-month delay in considering an immigration application did not amount to affirmative misconduct. In *I.N.S.* however, no regulation or statute was violated by the government and there was also justification for the administrative delay.

In *Schweiker v. Hansen,* 450 U.S. 785 (1981) incorrect advice given by a field representative of the Social Security Administration did not amount to affirmative misconduct. Most revealingly, the Supreme Court stated in *Schweiker* that "[a]t most, Connelly's [the government's] conduct *did not cause respondent to take action . . . or fail to take action,* . . . that respondent could not correct at any time." (Citations omitted) *Id.* at 789 [emphasis supplied]. Furthermore, the Supreme Court emphasized that the field representative's neglect only violated *the agency's claims manual and not a regulation. See Schweiker v. Hansen,* 450 U.S. 785. The contrast with the facts of this case could hardly be more striking, in that here the importer was irreparably injured as a result of an obvious disregard by the government of its own regulations and a statute.

The loss of revenue here is directly attributable to the government's failure to act in accordance with its own regulations and in accordance with a clear Congressional mandate. In this case the plaintiff has not acted in behalf of the public interest and thus has no right to resist the just effect of equitable estoppel.

In conclusion, this Court holds that the government's failure to act in accordance with the law equitably estopps it from obtaining the duties in question. The defendants' claims, for equitable recoupment as well as the government's obligation to the surety are not reached in this opinion because this action is resolved on more fundamental grounds.

/s/ JAMES L. WATSON
JAMES L. WATSON, Judge

DATED: March 14, 1985
New York, New York

UNITED STATES COURT OF INTERNATIONAL TRADE

Court No. 82-05-00594

UNITED STATES OF AMERICA,

Plaintiff,

vs.

FEDERAL INSURANCE COMPANY and COMETALS, INC.,

Defendant.

JUDGMENT

This case having been duly submitted for decision and the Court, after due deliberation, having rendered a decision herein; now, in conformity with said decision,

IT IS HEREBY ORDERED, ADJUDGED, and DECREED:

That plaintiff's motion for summary judgment is DENIED; and it is further

ORDERED that defendant's motion for summary judgment is GRANTED.

/s/ JAMES L. WATSON
Judge of the United States Court
of International Trade

Dated: New York, New York
March 14, 1985

APPENDIX D

Slip Op. 83-118

UNITED STATES COURT OF INTERNATIONAL TRADE

Before WATSON, Judge

Court No. 82-05-00594

UNITED STATES,

Plaintiff,

v.

FEDERAL INSURANCE COMPANY and COMETALS, INC.,

Defendants.

MEMORANDUM OPINION AND ORDER ON MOTION TO DISMISS

[Motion Granted in Part]
Decided November 15, 1983

J. Paul McGrath, Assistant Attorney General, Joseph I. Liebman, Attorney in Charge, International Trade Field Office (*Barbara M. Epstein*, attorney) for plaintiff.

Serko & Simon (*David Serko, Margaret H. Sachter, George S. Locker,* of counsel) for defendants.

WATSON, Judge: This opinion is limited to deciding the plaintiff's motion to dismiss defendants' counterclaims. The action itself was brought by the United States under 28 U.S.C. § 1582(2) and (3) for payment of duties and to recover on a bond posted to insure the payment of duties. The action was brought against Cometals, Inc., the importer of the merchandise and Federal Insurance Company, the surety under a general term bond posted by the importer. The action was brought after the importer's cus-

tomshouse broker, James Loudon & Co., Inc., failed to pay the duties and declared bankruptcy.

The defenses and counterclaims are generally based on claims that the government failed to adequately supervise the broker and failed to notify defendants of the broker's precarious financial condition. This assertedly amounted to tortious negligence or breach of an implied contract on the part of the government which caused financial loss to the importer and increased the risk to the surety. The counterclaims are said to arise under the Federal Tort Claims Act (28 U.S.C. §§2671 *et seq.*) the Tucker Act (28 U.S.C. §1491), the Administrative Procedure Act (5 U.S.C. §§701 *et seq.*), and the theory of equitable recoupment.

Plaintiff has moved to dismiss the counterclaims for failure to state a claim. In this opinion, the Court dismisses all but one, as being outside the counterclaim jurisdiction of the Court. The counterclaim for equitable recoupment appears to function much as a set-off, and to that extent its disposition is reserved for the decision on plaintiff's main claim.

The Administrative Procedure Act does not create an action for damages so it has no place as a counterclaim in this action. This Court has no jurisdiction over claims arising under the Federal Tort Claims Act (28 U.S.C. §1346(b)). *Bar Bea Truck Leasing Co. v. United States*, 4 CIT 70, 546 F. Supp. 558 (1982) *rev'd on other grounds*, 713 F.2d 1563 (C.A.F.C. 1983). Consequently, a counterclaim under that Act is *a fortiori* outside the jurisdiction of the Court.

The remaining counterclaim is brought under the Tucker Act (28 U.S.C. §1491). To dispose of that claim, grounded in breach of an express or implied contract, it is sufficient to note that it cannot come within the counterclaim jurisdiction of the Court because it does not meet the statutory requirements.

The terms of 28 U.S.C. §1583[1] (and Rule 13 of the Court Rules, which reflect the statute) limit counterclaims to claims which involve the imported merchandise or to claims to recover upon a bond or customs duties. It is clear that the "Tucker Act" claim does not belong to the latter. It is further clear that it does not involve the imported merchandise within the meaning of the statute. This reasoning is unavoidable because if "involvement" with the imported merchandise is not sufficient to support a counterclaim by the government to collect customs duties (thus requiring a special mention to permit those counterclaims) the somewhat more remote dispute about the government's obligations to supervise brokers and inform importers and sureties certainly does not "involve the imported merchandise" within the meaning of the counterclaim provision.

For the reasons expressed above, the defendant's counterclaims, with the exception of the claim for equitable recoupment, are hereby DISMISSED.

/s/ JAMES L. WATSON
James L. Watson, Judge

DATED: November 15, 1983
New York, New York

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[1] Sec. 1583. *Counterclaims, cross-claims, and third-party actions:*

In any civil action in the Court of International Trade, the Court shall have exclusive jurisdiction to render judgment upon any counterclaim, cross-claim, or third-party action of any party, if (1) such claim or action involves the imported merchandise that is the subject matter of such civil action, or (2) such claim or action is to recover upon a bond or customs duties relating to such merchandise.

APPENDIX E

19 U.S.C. § 1641

§ 1641. Customhouse brokers

Regulations for licensing

(a) The Secretary of the Treasury may precribe rules and regulations governing the licensing as customhouse brokers of citizens of the United States of good moral character, and of corporations, associations, and partnerships, and may require as a condition to the granting of any license, the showing of such facts as he may deem advisable as to the qualifications of the applicant to render valuable service to importers and exporters. No such license shall be granted to any corporation, association, or partnership unless licenses as customhouse brokers have been issued to at least two of the officers of such corporation or association, or two of the members of such partnership, and such licenses are in force. Any license granted to any such corporation, association, or partnership shall be deemed revoked if for any continuous period of more than sixty days after the issuance of such license there are not at least two officers of such corporation or association or two members of such partnership who are qualified to transact business as customhouse brokers. Except as provided in subdivision (c) of this section, no person shall transact business as a customhouse broker without a license granted in accordance with the provisions of this subdivision, but nothing in this section shall be construed to authorize the requiring of a license in the case of any person transacting at a customhouse business pertaining to his own importations.

Revocation or suspension; appeal

(b) The appropriate officer of the customs may at any time, for good and sufficient reasons, serve notice in writing upon any customhouse broker so licensed to show cause why said license shall not be revoked or suspended, which

notice shall be in the form of a statement specifically setting forth the ground of complaint. The appropriate officer of customs shall within ten days thereafter notify the customhouse broker in writing of a hearing to be held before him within five days upon said charges. At such hearing the customhouse broker may be represented by counsel, and all proceedings including the proof of the charges and the answer thereto, shall be presented, with the right of cross-examination to both parties, and a stenographic record of the same shall be made and a copy thereof shall be delivered to the customhouse broker. At the conclusion of such hearing the appropriate officer of customs shall forthwith transmit all papers and the stenographic report of the hearing, which shall constitute the record of the case, to the Secretary of the Treasury for his action. Thereupon the said Secretary of the Treasury shall have the right to revoke or suspend the license of any customhouse broker shown to be incompetent, disreputable, or who has refused to comply with the rules and regulations issued under this section, or who has, with intent to defraud, in any manner willfully and knowingly deceived, misled, or threatened any importer, exporter, claimant, or client, or prospective importer, exporter, claimant, or client, by word, circular, letter or by advertisement.

An appeal may be taken by any licensed customhouse broker from any order of the Secretary of the Treasury suspending or revoking a license. Such appeal shall be taken by filing, in the court of appeals of the United States within any circuit wherein such person resides or has his principal place of business, or in the United States Court of Appeals for the District of Columbia, within sixty days after the entry of such order, a written petition praying that the order of the Secretary of the Treasury be modified or set aside in whole or in part. A copy of such petition shall be forthwith transmitted by the clerk of the court to the Secretary of the Treasury, or any officer designated by him for that purpose, and thereupon the Secretary of

the Treasury shall file in the court the record upon which the order complained of was entered, as provided in section 2112 of Title 28. Upon the filing of such petition such court shall have exclusive jurisdiction to affirm, modify, or set aside such order, in whole or in part. No objection to the order of the Secretary of the Treasury shall be considered by the court unless such objection shall have been urged before the appropriate officer of customs or unless there were reasonable grounds for failure so to do. The finding of the Secretary of the Treasury as to the facts, if supported by substantial evidence, shall be conclusive. If any party shall apply to the court for leave to adduce additional evidence, and shall show to the satisfaction of the court that such additional evidence is material and that there were reasonable grounds for failure to adduce such evidence in the proceeding before the appropriate officer of customs, the court may order such additional evidence to be taken before the appropriate officer of customs and to be adduced upon the hearing in such manner and upon such terms and conditions as to the court may seem proper. The Secretary of the Treasury may modify his findings as to the facts by reason of the additional evidence so taken, and he shall file with the court such modified or new findings, which, if supported by substantial evidence, shall be conclusive, and his recommendation, if any, for the modification or setting aside of the original order. The judgment and decree of the court affirming, modifying, or setting aside, in whole or in part, any such order of the Secretary of the Treasury shall be final, subject to review by the Supreme Court of the United States upon certiorari or certification as provided in section 1254 of Title 28. The commencement of proceedings under this subsection shall, unless specifically ordered by the court, operate as a stay of the Secretary of the Treasury's order.

Prior licenses

(c) Licenses issued under section 415 of this title or under the provisions of subdivision (a) of this section prior to August 26, 1935, shall continue in force and effect, subject to suspension and revocation as provided in subdivision (b) of this section.

Regulations by Secretary

(d) The Secretary of the Treasury shall prescribe such rules and regulations as he may deem necessary to protect importers and the revenue of the United States, and to carry out the provisions of this section, including rules and regulations requiring the keeping of books, accounts, and records by customhouse brokers, and the inspection thereof, and of their papers, documents, and correspondence by, and the furnishing by them of information relating to their business to, any duly accredited agent of the United States.

APPENDIX F

19 U.S.C. § 1648

§ 1648. Uncertified checks, United States notes, and national bank notes receivable for customs duties

Customs officers may receive uncertified checks, United States notes, and circulating notes of national banking associations in payment of duties on imports, during such time and under such rules and regulations as the Secretary of the Treasury shall prescribe: but if a check so received is not paid the person by whom such check has been tendered shall remain liable for the payment of the duties and for all legal penalties and additions to the same extent as if such check had not been tendered.

APPENDIX G

28 U.S.C. § 1583

§ 1583. Counterclaims, cross-claims, and third-party actions

In any civil action in the Court of International Trade, the court shall have exclusive jurisdiction to render judgment upon any counterclaim, cross-claim, or third-party action of any party, if (1) such claim or action involves the imported merchandise that is the subject matter of such civil action, or (2) such claim or action is to recover upon a bond or customs duties relating to such merchandise.

APPENDIX H

19 C.F.R. § 24.1(3) (1980)

§ 24.1 Collection of Customs duties, taxes, and other charges.

(a) Except as provided in paragraph (b) of this section, the following procedure shall be observed in the collection of Customs duties, taxes, and other charges:

(3) An uncertified check drawn by an interested party on a national or state bank or trust company of the United States or a bank in Puerto Rico or any possession of the United States if such checks are acceptable for deposit by a Federal Reserve bank, branch Federal Reserve bank, or other designated depositary shall be accepted if there is on file with the district director an entry bond or other bond to secure the payment of the duties, taxes, or other charges, or if a bond has not been filed, the organization or individual drawing and tendering the uncertified check has been approved by the district director to make payment in such manner. In determining whether an uncertified check shall be accepted in the absence of a bond, the district director shall use available credit data obtainable without cost to the Government, such as that furnished by banks, local business firms, better business bureaus, or local credit exchanges, sufficient to satisfy him of the credit standing or reliability of the drawer of the check.

APPENDIX I

19 C.F.R. § 111.27 (1980)

§ 111.27 Audit or inspection of books and papers.

The Regional Director, Regulatory Audit, shall make such audit or inspection of the books and papers required by this subpart to be kept and maintained by a broker as may be necessary to enable the district director and other proper officials of the Treasury Department to determine whether or not the broker is complying with the requirements of this part. Furthermore, the Regional Director, Regulatory Audit, and/or the special agent in charge, may inspect such books and papers to obtain information regarding specific Customs transactions for the purpose of protecting importers or the revenue of the United States. The Regional Director, Regulatory Audit, and the special agent in charge conducting an audit or inspection under this section shall submit a report of the findings to the Commissioner and the district director.

APPENDIX J

19 C.F.R. § 111.29 (1980)

§ 111.29 Diligence in correspondence and paying monies.

Each broker shall exercise due diligence in making financial settlements, in answering correspondence, and in preparing or assisting in the preparation and filing of documents relating to any matter handled by him as a broker. Funds received by a broker from a client for payment of duty, tax, or other debt or obligation owing to the Government shall be paid to the Government within 30 days from date of receipt or date due, whichever is later. Each broker shall within 60 days account to clients for funds received for them from the Government, or received from a client in excess of the governmental or other charges properly payable in response to the client's business. He shall account to all other persons within 30 days of receipt for all funds advanced by a client for payment of any charges, debts, or obligations due such other persons.